

Weekly Macro & Markets View

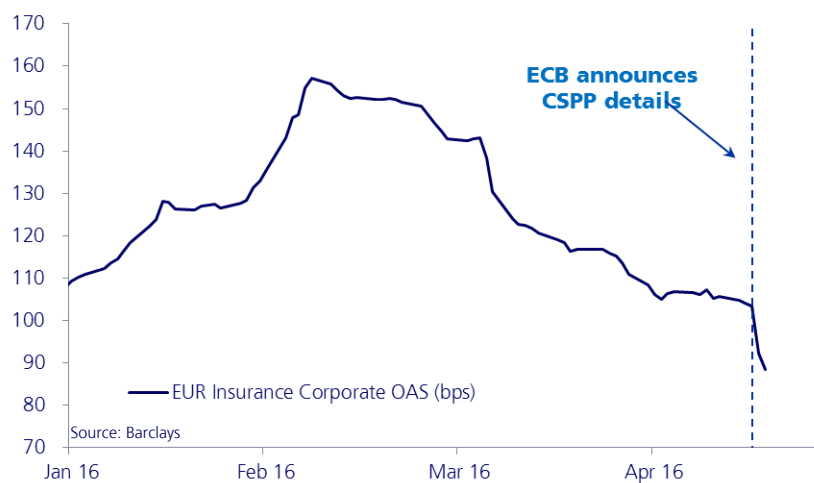
Highlights

- ECB unveils technical details of its Corporate Sector Purchase Program (CSPP)
- Argentina successfully issues the largest ever EM bond issue
- Oil prices sustain a rally despite Doha talks ending without an agreement

Our view

- The ECB's CSPP should be very supportive for global credit markets
- Argentina's new bond issue should be positive for the country and the EM asset class
- The resilience of oil prices continues to support risky assets

Technical details of the ECB's CSPP reinforce our constructive stance on credit



Credit markets rallied hard last week, outpacing gains in other risky assets. While we have been constructive on credit, last week's ECB meeting reaffirmed our conviction, as we believe that a compression of credit spreads is now an implicit policy objective.

The technical details of the ECB's Corporate Sector Purchase Program (CSPP) were more supportive than the market was anticipating. The ECB will be targeting most of the Euro denominated non-bank corporate debt universe. It will purchase securities that have maturities between six months and thirty years, in a size of as much as 70% of the bond issue (with some exceptions where this may potentially be limited to 33%), in both primary and secondary markets. While this captures most of the eligible universe in most investment grade indices, the ECB could also potentially purchase so called 'crossover' bonds, which have both investment grade and high yield ratings. It was clarified that the ECB will be buying non-bank financial issuer's debt, which includes debt of the insurance sector. This caused insurer debt spreads to rally sharply. At the same time, the ECB could buy debt of issuers whose ultimate parent may not be incorporated in the Eurozone, opening the door to several US issuers. This would further improve the supply-demand technicals for US credit, which are already improving due to waning M&A activity.

Eurozone: Lending survey and other data confirm recovery still on track

As well as the ECB meeting, last week also saw various data confirming the ongoing recovery in the Eurozone, though the pace of growth remains modest for now. The Eurozone flash composite PMI survey came in at 53.0 for April, virtually unchanged from March, and consistent with growth of 0.3-0.4% quarter on quarter. At the country level, the German manufacturing PMI was stronger, suggesting export demand is picking up. Separately, the latest

ECB lending survey for Q1 showed that despite the financial market volatility over the quarter, banks continued to ease lending standards for corporates. Eurozone banks also reported that net loan demand from corporates grew, though at a slower pace than the previous quarter. Finally, analyst sentiment, as measured by the ZEW survey, also picked up in April, in line with the improvement in risk assets over the past few weeks.

US: Initial jobless claims fall to the lowest level since 1973

Housing data were mixed as housing starts and building permits were lower while existing home sales were better than expected in March. The Philadelphia Fed Business Outlook and the Markit Manufacturing PMI both indicate renewed weakness in the manufacturing sector after the pick-up in March. However, with initial jobless claims falling to the lowest level since 1973, the US economy as a whole remains in a decent shape. The earnings season gained traction last week with a

quarter of the reports now published. While the overall beat/miss-ratio is roughly in line with historic averages, earnings are currently still more than 8% lower than last year and the latest batch of data from large IT companies including Microsoft and Alphabet was not inspiring. Accordingly, the NASDAQ was underperforming the broader market last week.

Japan: Repercussions from the Kumamoto earthquake

The two major earthquakes in Kumamoto prefecture on April 14 and 16 are not comparable to the Great East Japan Earthquake in 2011 or the Great Hanshin Earthquake in 1995, both in terms of human casualties and the nationwide economic impact. The share of the most affected prefectures Kumamoto and Oita in Japan's GDP adds up to about 2%. However, nationwide supply chain disruptions have been reported particularly for the auto and semiconductor industries,

with Japan's biggest auto company having had to stop its automobile production. We believe the impact could add up to a reduction in industrial production of 0.3 percentage points in Q2. Consumer sentiment and local tourism will also be negatively affected in the short term.

The damage to the capital stock should enable more fiscal spending, while TPP negotiations and plans for Lower House elections will likely be postponed.

Argentina: Biggest EM bond primary issue ever

Argentina successfully raised \$16.5 billion last week, in an issue that was 4 times oversubscribed. It is its first sale since the 2001 default and the biggest EM primary issuance ever, doubling the weight of Argentina in the global emerging markets index. The government was able to reduce the offered yield by 50bps and the average was 7.2% across four tranches. Proceeds will be used to pay the holdouts and reduce the Treasury dependence on central bank transfers. With a 30% debt-to-GDP ratio at

the end of 2015, the country is underleveraged. Debt issuance is part of the macro rebalancing process where inflation and fiscal deficit will take center stage now. We expect significant capital inflows in an economy starved for investments as the cost of capital has significantly cheapened. The door is now open for provinces and corporates to tap the markets.

Bond yields rise but remain stretched

Treasury yields rose firmly last week, with the 10yr up 13bps to 1.89%, as inflation breakevens responded positively to higher oil prices. An extremely benign Fed hiking cycle of only one rate hike per year also continues to be priced in, limiting the potential for dovish repricing. It was encouraging that Bund yields also rose, with investors shifting focus to fundamentals once April's tight net supply and higher pace of QE purchases were underway. Bund yields are still stretched

though, and could rise further near term, particularly as inflation expectations are stuck at a very low level. We also anticipate the ECB to shift a significant amount of QE purchases to the corporate sector programme which should help alleviate some of the pressures, though distortions will remain large.

What to Watch

- The US and the Eurozone will be reporting their Q1 GDP. While US growth is expected to be weak, Eurozone growth should be stronger.
- While we do not expect any action at this week's Fed meeting, it will be crucial whether the FOMC is preparing the markets for a rate hike in the summer. The focus will be the Fed's interpretation of the recent improvement of global economic and financial conditions.
- We expect the Bank of Japan to expand its QE program by raising its ETF buying target significantly during its policy board meeting on Wednesday/Thursday.

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